

## Message Text

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PAGE 01 ABU DH 01558 01 OF 02 241252Z  
ACTION NEA-10

INFO OCT-01 EUR-12 ISO-00 AID-05 CIAE-00 COME-00 EB-07  
FRB-03 INR-07 NSAE-00 USIA-06 TRSE-00 XMB-02  
OPIC-03 SP-02 LAB-04 EPG-02 SIL-01 OMB-01 PA-01  
PRS-01 /068 W  
-----241305Z 020861 /50

R 241220Z MAY 77  
FM AMEMBASSY ABU DHABI  
TO SECSTATE WASHDC 6127  
INFO AMEMBASSY JIDDA  
AMEMBASSY KUWAIT  
AMEMBASSY TEHRAN  
AMEMBASSY LONDON  
AMEMBASSY MUSCAT  
AMEMBASSY MANAMA  
AMEMBASSY DOHA

LIMITED OFFICIAL USE SECTION 1 OF 2 ABU DHABI 1558

E.O. 11652: N/A  
TAGS: EFIN, TC  
SUBJ: UAE CURRENCY BOARD ANNOUNCES CREDIT SQUEEZE  
  
REF: ABU DHABI A-8, ABU DHABI A-20

SUMMARY: UAE CURRENCY BOARD PUBLICLY ANNOUNCED MAY 23 NEW MEASURES TO REDUCE INCREASE IN CREDIT CREATED BY BANKING SYSTEM AND TO PUT BANKING SYSTEM ON MORE SOUND BASIS. TWO LOCAL BANKS (ONE OF WHICH HAS MINORITY U.S. OWNERSHIP AND MANAGEMENT CONTRACT) HAS BEEN DENIED CLEARING PRIVILEGES. RESULTS OF CREDIT SQUEEZE LIKELY TO CURB INFLATION AND SPECULATION, WEAKEN BANKS DEPENDENT TOTALLY ON LOCAL MARKET AND ENHANCE COMPETITIVE POSITION OF MAJOR BANKS. END SUMMARY.

1. UAE CURRENCY BOARD HAS TAKEN STRONG ACTION TO CURB BANK  
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CREDIT EXPANSION (WHICH INCREASED 85 PERCENT IN 1976) AND TO DISCIPLINE UAE. REPAIRS HAVE INDICATED UNSETTLED STATE OF BANKING SECTOR HERE IN RECENT MONTHS.

CURRENCY BOARD GM RON SCOTT ANNOUNCED PUBLICLY MAY 23 THAT UAE PRESIDENT ZAYED HAD AUTHORIZED FOLLOWING MEASURES: QUOTE:  
1) NO FURTHER BANKS, BANK BRANCHES OR ANY OTHER FORM OF

FINANCIAL INSTITUTION WILL BE ALLOWED TO OPEN IN THE U.A.E.  
UNTIL FURTHER NOTICE;

2) IN ADDITION TO BANKS, ALL OTHER FINANCIAL INSTITUTIONS  
WILL BE BROUGHT UNDER THE CONTROL OF THE CURRENCY BOARD;

3) THE PERCENTAGE OF BANKS DIRHAM DEPOSITS REQUIRED TO BE  
HELD WITH THE CURRENCY BOARD WILL BE INCREASED FROM 5 PERCENT TO  
7 1/2 PERCENT;

4) THE PROPORTION OF A BANKS OWN FUNDS E.G. CAPITAL AND  
RESERVES TO TOTAL LIABILITIES SHOULD NOT BE LESS THAN A RELATION-  
SHIP OF 1 TO 15. THIS REQUIREMENT TO APPLY EQUALLY TO BRANCHES  
AND SUBSIDIARIES OF FOREIGN BANKS OPERATING IN THE U.A.E.

5) DIRECTIVES WILL BE GIVEN TO INDIVIDUAL BANKS CONCERNING THE  
PERCENTAGE RELATIONSHIP BETWEEN THEIR TOTAL ADVANCES AND THEIR  
TOTAL DEPOSITS EXCLUDING INTER BANK DEPOSITS

3. CURRENCY BOARD STRESSES THAT MEASURES TO BE IMPLEMENTED SO  
AS TO CAUSE AS LITTLE DISRUPTION AS POSSIBLE TO SYSTEM. MORATO-  
RIUM ON NEW OPERINGS IS IMMEDIATE, WHILE BRINGING OTHER FINANCIAL  
INSTITUTIONS (INCLUDING NEWLY CREATED INVESTMENT COMPANIES)  
UNDER CURRENCY BOARD CONTROL WILL BE PROGRESSIVE, AS CURRENCY  
BOARD PERSONNEL CAPABILITIES ARE INCREASED. REGARDING RAISED  
RESERVE REQUIREMENTS, FIRST FIVE PER CENT HELD WITH CURRENCY  
BOARD WILL BE INTEREST FREE; ADDITIONAL TWO AND A HALF PERCENT  
WILL BE INTEREST-BEARING EITHER CASH AT FOUR PER CENT OR BONDS  
PURCHASED FROM CURRENCY BOARD PORTOLIO (LAST YEAR BOARD PARTICI-  
PATED IN AND IS NOW HOLDING DIRHAM BOND OFFERINGS IN THE SEVEN  
TO NINE PERCENT RANGE FROM ALGERIAN NATIONAL SHIPPING CO. AND GOV-  
ERNMENT BANKS IN YOGOSLAVIA, SOUTH KOREA, AND TUNISIA).

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3. REQUIREMENT THAT RATIO OF CAPITAL AND RESERVES TO TOTAL  
LIABILITIES SHOULD NOT EXCEED ONE TO FIFTEEN WILL BE EFFECTED  
GRADUALLY. CONSOLIDATED COMMERCIAL BANK RATIO AS OF 9/76 WAS 43  
TO ONE. CHANGE WILL BE DRAMATIC IN SOME CASES AND POLICY WILL  
PROCEED ON CASE BY CASE BASIS. NATIONAL BANK OF ABU DHABI RATIO  
IS NOW ONE TO FIFTY-SEVEN. BOARD IS EXPECTED TO BE TOUGH WITH  
INTERNATIONAL BANKS WHICH CAN FREELY TRANSFER DEPOSITS AND LOANS  
IN AND OUT OF COUNTRY IN ORDER TO ACHIEVE DESIRED RATIO.  
BANKS DEPENDENT ON LOCAL MARKET TO RAISE MORE CAPITAL OR DECREASE  
TOTAL LIABILITY WILL HAVE MORE DIFFICULT TASK AND BOARD EXPECTED  
TO GO EASIER ON THEM.

4. BOARD WILL PROCEED ON A CASE BY CASE BASIS IN ITS DESIRE TO  
ESTABLISH A "PERCENTAGE RELATIONSHIP" BETWEEN TOTAL ADVANCES  
AND TOTAL DEPOSITS EXCLUDING INTER-BANK DEPOSITS. NO CONCRETE IN-  
FORMATION IS YET AVAILABLE ON THIS ASPECT OF PROGRAM; HOWEVER INTER-  
BANK DEPOSITS ARE SUBSTANTIAL IN UAE. (ROUGH ESTIMATES ARE THAT  
NATIONAL BANK OF ABU DHABI HAS MORE THAN \$300 MILLION DOLLARS IN  
LOCAL TIME DEPOSITS IN DIFFERENT BANKS IN UAE). BOARD IS OVBIOUSLY

INTERESTED IN PARING THIS INCENTIVE TO CREDIT EXPANSION. OTHER ASPECTS OF PROGRAM ARE RE-EMPHASIS OF BOARD'S ABILITY TO AUDIT BANKS AT ANY TIME. NO BANK, TO OUR KNOWLEDGE, HAS EVER BEEN AUDITED AT BOARD'S REQUEST. ADDITIONALLY, BOARD IS SUSPENDING ALL LOAN FACILITIES TO BANKS. PREVIOUSLY, BANKS WITH LIQUIDITY PROBLEMS COULD ASK FOR AN D EASILY GET LOANS. NOW, EVEN BANKS WITH PREVIOUS BOARD COMMITMENTS FOR LOANS MAY HAVE THEM WITHDRAWN.

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5. TWO BANKS ARE NOW IN TROUBLE AND HAVE BEEN CLOSED FOR LAST FIVE DAYS SINCE BOARD REFUSING CLEARING FACILITIES: JANATA BANK (BANGLADESH OWNED) AND AJMAN ARAB BANK (20 PERCENT U.S. OWNERSHIP AND MANAGEMENT CONTRACT BY WFC CORP. OF CORAL GABLES, FLA. AND NEW YORK CITY). STORY BEHIND THESE BANKS DIFFICULTIES HAS NOT YET SURFACED. CURRENCY BOARD IS NOT YET DECIDED ON COURSE OF ACTION.

6. COMMENT: EXPANSION OF SYSTEM WAS GETTING OUT OF HAND. BANKS HAVE BEEN GETTING INVOLVED HEAVILY IN SPECULATING IN REAL ESTATE AND GENERALLY INDULGING IN ENTREPRENEURSHIP RATHER THAN NORMAL BANKING PRACTICES. BANKING SYSTEM EFFECT OF THIS OPERATING WILL SURELY BE TO WEAKEN THE WEAK BANKS AND STRENGTHEN INTER-

NATIONAL ONES. MORE GENERAL EFFECT WILL BE TO THROW SHOCK INTO  
BOOM-TOWN MENTALITY WHICH HAS PUFFED UP EXPECTATIONS HERE BEYOND  
THAT WHICH ANY SEMBLANCE OF ADHERENCE TO LAWS OF ECONOMICS WOULD  
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PERMIT.  
DICKMAN

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## Message Attributes

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**To:** STATE  
**Type:** TE  
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